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Nos. 81-31, 81-228 and 81-455

IN THE

Supreme Court of the United States

October Term, 1981

STATE OF CALIFORNIA, *et al.*,

Appellants,

vs.

GRACE BRETHREN CHURCH, *et al.*,

Appellees.

On Appeal From the United States District Court for the Central District of California.

Amended Brief of Appellants, State of California, California Employment Development Department, and the Director of the California Employment Development Department.

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Questions Presented.

1. Whether the Court's jurisdiction is properly invoked under 28 U.S.C. § 1252.

2. Whether 26 U.S.C. § 3309(b)(1) and California Unemployment Insurance Code § 634.5(a) as interpreted and applied result in excessive entanglement of the state with religion in the benefit eligibility determination process with respect to employees of religious schools and thus are incompatible with the religion clauses of the First and Fourteenth Amendments.

3. Whether a violation of the Free Exercise Clause results from the inclusion of employees of religious schools in the unemployment compensation program.

4. Whether a denial of equal protection results from the inclusion of employees of unaffiliated religiously oriented schools in the unemployment compensation tax program.

5. Whether 28 U.S.C. § 1341 deprived the District Court of jurisdiction of this action.[1]

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[1]The plaintiffs in Case No. CV 79-93MRP (hereinafter referred to as the "Grace Brethren case") are:

Grace Brethren Church of Long Beach, California, and its pastor, Rev. David L. Hocking; Calvary Cross Church of the Highlands of San Bruno, California, and its pastor, Rev. Donald B. Sheley; Scott Memorial Baptist Church of San Diego, California, and its pastor, Rev. Tim LaHaye; Christian Unified Schools of San Diego, an incorporated association of five fundamentalist schools with a central office in El Cajon, California; Redwood Christian Schools, an incorporated association of four fundamentalist schools with a central office in Castro Valley, California; Sidney and Patricia Bowen of Compton, California, whose children attend Grace Christian Schools, an affiliate of plaintiff Grace Brethren Church; Peter and Sue Farrelly of Pacifica, California, whose children attend Highlands Academy, an affiliate of plaintiff Calvary Cross Church of the Highlands; William and Janet Tschantz of LaMesa, California, whose children attend plaintiff Christian Unified Schools of San Diego; Arthur and Cheryl Brandwood of Hayward, California, whose children attend plaintiff Redwood Christian Schools; Stanley Eddington of San Lorenzo, California, a teacher at plaintiff Redwood Christian Schools; R. Florence Murti of Daly City, California, a teacher at Highlands Academy; and R. Suzanne Royer of Long Beach, California, a teacher at Grace Christian Schools.

The defendants in the "Grace Brethren Case" — Case No. 79-93MRP are:

The State of California; The California Employment Development Department; The Director of the California Employment Development Department; The United States of America; The United States Department of Labor; and the United States Secretary of Labor.

The plaintiffs in Case No. CV 79-162MRP (hereinafter referred to as the "Lutheran case") are:

The Lutheran Church-Missouri Synod, a nonprofit membership corporation on behalf of the eighty-five of its member churches which operate primary or secondary schools; St. John's Lutheran Church, a member of plaintiff Lutheran Church-Missouri Synod and operator of a primary school in Orange, California; and Vivadell Keiser, a teacher at the primary school operated by plaintiff St. John's Lutheran Church.

The named defendants in the "Lutheran Case" — Case No. CV 79-162MRP are:

The California Employment Development Department; The Director of the California Employment Development Department; and The United States Secretary of Labor.

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OPINIONS BELOW.

The Opinion of the United States District Court for the Central District of California for both cases is entitled Second Supplemental Opinion and is not presently reported. A copy of said Opinion is attached to the State of California's Jurisdictional Statement as Appendix A, pp. 1-44. (State J.S. App. A, pp. 1-44.) The Order and Judgment in the Grace Brethren case appears as Appendix B to the State's Jurisdictional Statement. (State J.S. App. B, pp. 45-48.) The Order and Judgment in the Lutheran case appears as Appendix C to the State's Jurisdictional Statement. (State J.S. App. C, pp. 49-51.) The District Court's two earlier Opinions at the preliminary injunction stage entitled Opinion and Supplemental Opinion are likewise not presently re-

ported. (State J.S. App. D, pp. 51-70 and State J.S. App. E, pp. 71-79.) Copies of the corresponding Orders appear as Appendices F and G, respectively, to the State's Jurisdictional Statement. (State J.S. App. F, pp. 80-81 and State J.S. App. G, pp. 82-83.)

JURISDICTION.

Both suits were brought in the District Court[2] on behalf of the respective plaintiffs for injunctive and declaratory relief under the authority of 28 U.S.C. § 1331 as the suits involved substantial questions as to the interpretation and constitutionality of the Federal Unemployment Tax Act. ("FUTA"; 26 U.S.C. §§ 3301, *et seq.*) Jurisdiction was further invoked in the Grace Brethren case under 42 U.S.C. § 1983, 28 U.S.C. §§ 1343, 1346, 2201 and 2202.

The judgments of the District Court were entered on April 6, 1981. (State J.S. App. B, pp. 45-58; App. C, pp. 49-51.) The State appellants filed a Notice of Appeal to this Court from each judgment on May 6, 1981. (State J.S. App. H, pp. 84-87; App. I, pp. 88-91.) The jurisdiction of this Court is invoked under 28 U.S.C. § 1252.

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED.

First Amendment, United States Constitution:

> "Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; or abridging the freedom of speech, or of the press; or the right of the people peaceably to assemble,

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[2]The Lutheran case was originally brought in the Superior Court of the State of California for the County of Los Angeles and was subsequently removed by the federal defendants to the United States District Court for the Central District of California pursuant to 28 U.S.C. §§ 1441 and 1442. The Lutheran case was ultimately consolidated with the Grace Brethren case in that court.

and to petition the Government for a redress of grievances."

Fifth Amendment, United States Constitution:

"[Section 1.] No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a grand jury, except in cases arising in the land or naval forces, or in the militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

Fourteenth Amendment, United States Constitution:

"Section 1. All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws."

26 U.S.C. § 3309(b):

"This section shall not apply to service performed —

(1) in the employ of (A) a church or convention or association of churches, or (B) an organization which is operated primarily for religious purposes and which is operated, supervised, controlled, or principally supported by a church or convention or association of churches; . . ."

California Unemployment Insurance Code § 634.5 (West Supp. 1981):

> "Notwithstanding any other provision of this code or any other code or law, no provision of this code or any other code or law excluding service from 'employment' shall apply to any public entity defined by Section 605 or to any nonprofit organization described by Section 608, except as provided by this section. With respect to any public entity defined by Section 605 or any nonprofit organization described by Section 608, 'employment' does not include service excluded under Sections 629, 631, 635, and 639 to 648, inclusive, or service performed in any of the following:
>
> (a) In the employ of (1) a church or convention or association of churches or (2) an organization which is operated primarily for religious purposes and which is operated, supervised, controlled, or principally supported by a church or convention or association of churches . . ."

28 U.S.C. § 1341 provides:

> "The district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State."

STATEMENT OF THE CASE.

This litigation involves the challenge by various California churches, religiously oriented schools and individuals to the coverage of both church and school employees under the federal-state unemployment compensation tax program.[3]

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[3]The plaintiffs will be referred to as the "Grace Brethren appellees" and "Lutheran appellees" when separately discussed and simply "appellees" otherwise.

Appellees sought both declaratory and injunctive relief against the State[4] and the United States[5] The dispute arose chiefly between the appellees and the United States over whether services performed at schools operated by the appellees should be subject to unemployment taxation.[6]

The appellees contended and sought a declaration that such services were not subject to unemployment taxation on purely statutory grounds and in the alternative on the grounds that to impose unemployment insurance coverage upon them would be violative of their rights protected by the First, Fifth and Fourteenth Amendments to the Constitution of the United States.

The State agreed with the position of the appellees insofar as they sought declaratory relief on the purely statutory grounds and in fact cross-claimed against the United States seeking comparable declaratory relief. However, the State disagreed with the declaratory relief sought on any of the constitutional grounds.

The appellees also sought to enjoin the collection of unemployment information and tax, as well as disability information and tax by the State and to enjoin the United States from taking any action to compel the State to collect the unemployment insurance tax. The grounds were the

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[4]"State" refers to State of California, California Employment Development Department and the Director of the California Employment Development Department.

[5]"United States" refers to the United States of America, the United States Department of Labor and the United States Secretary of Labor.

[6]It should be noted that disability taxes under California law were also involved in these actions since in California, covered services for unemployment insurance purposes are the same as covered services for disability insurance purposes. California Unemployment Insurance Code § 2606. The issue in this appeal is however limited to the unemployment insurance aspect of the case.

same as those alleged in support of the request for declaratory relief.

The State opposed the issuance of injunctive relief on any grounds in that California law prohibits the enjoining of the collection of a tax. California Constitution, Article XIII, Section 32. The United States opposed all relief and filed both a Motion To Dismiss the appellees' Complaints and a Motion To Dismiss the State's Cross-Claim.

In opinions and orders filed on September 21, 1979, and June 2, 1980, (State J.S. App. D, E, F and G, pp. 51-83) the District Court granted the United States' Motion To Dismiss the State's Cross-Claim, denied the United States' Motion To Dismiss the appellees' complaints and granted appellees' motion for preliminary injunction against the State alone for all but two of the appellees.[7] The State

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[7]The District Court separated the employees who perform services for the schools involved herein into three categories:

Category 1: Those who are in the employ of a church or convention or association of churches.

Category 2: Those who are in the employ of a separate corporation formed by a church or a convention or association of churches.

Category 3: Those who are in the employ of a corporation which is operated primarily for religious purposes, but which is not operated, supervised, controlled or principally supported by a church or convention or association of churches, *i.e.*, an independent, non-church affiliated religious school.

(State J.S. App. E, p. 71.)

The two appellees who were not successful at the preliminary injunction stage were Redwood Christian Schools and Christian Unified Schools of San Diego. These were the only "category 3" religious organizations involved in the case. However, there was testimony by Mr. Ellis P. Murphy, director of legislative and legal services for the Association of Christian Schools International that approximately twenty (20) percent of its member schools in California (636) are "category 3" types. (R.T., p. 120 — R.T. refers to Reporter's Transcript of proceedings before Hon. Mariana R. Pfaelzer on August 12-13, 1980.) Furthermore, it was estimated that there are currently (Fall, 1979) 1589 religiously related schools in California. (State's Notice of Motion; Motion For Order Establishing Class Action, etc., p. 20.)

appealed to the Ninth Circuit from the Order granting the United States' Motion To Dismiss the State's Cross-Claim and later withdrew said appeal. (Case Nos. 79-3784 and 79-3785.) The United States also appealed the District Court's preliminary rulings to the Ninth Circuit. Its appeal was from the Order granting appellees' request for a preliminary injunction. This appeal was likewise dismissed. (Case Nos. 79-3763 and 79-3764.)

At the preliminary injunction stage, although concluding that the Secretary of Labor's interpretation of 26 U.S.C. § 3309(b) imposed upon the States and embodied in Program Letter No. 39-78 (State J.S. App. J, pp. 92-96) was both erroneous as a matter of statutory construction and as inconsistent with the constitutional prohibition against excessive state entanglement with religion, the District Court did not pass on the precise question presented by the State's appeal. (State J.S., p. i.)

Benefit Eligibility Hearings.

The question raised in the State's appeal was first considered at length at the subsequent trial. The appellees presented no evidence to demonstrate that there ever had been a benefit eligibility determination hearing with respect to an employee of a church-related school. Moreover, there was no evidence presented by the appellees that there had ever been a benefit eligibility hearing where the issues either involved a dispute concerning a church or other religious organization with respect to the reasons for discharge of the employee by the church or religious organization or a dispute which required an inquiry into church doctrine.

The only evidence at the trial pertaining to the issue was hypothetical questions posed to two witnesses for the United

States and their responses thereto.[8] Although each witness was experienced in the field of benefit eligibility determination hearings and in fact supervised State programs, both witnesses testified that they had never conducted, attended nor read a transcript of a benefit eligibility hearing from any State where the issues involved a dispute between a church and church employee with respect to the reasons for discharge of the employee by the church. (R.T., p. 165, lines 6-12; R.T., p. 166, lines 13-17; R.T., p. 228, line 15; R.T., p. 231, line 13; R.T., p. 231, line 14; R.T., p. 232, line 14.)

The first federal witness, Mr. Carter, testified that his job is to furnish technical assistance to the states in interpreting federal law and requirements in predetermination benefit eligibility hearings. (R.T., pp. 154-155.) He testified that he conducts training courses in this area for the states (R.T., p. 155) and that there are general federal guidelines provided to the states for proceeding when the issue is misconduct or voluntary leaving. (R.T., p. 175.) However, he continued that there are no particular federal guidelines with respect to misconduct in situations arising in religious schools. (R.T., p. 175.) Mr. Carter indicated that ultimately the decision would be a matter of state law and policy, (R.T., pp. 175, 214-216) and further, that he did not know the specific definition of misconduct in California (R.T., p. 202).[9] Finally, Mr. Carter testified on cross-examination that in 1979 approximately 4 million cases were adjudicated

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[8]The two witnesses were Ernest L. Carter and Bernard Streett. Their testimony appears at R.T., pp. 153-221, and R.T., pp. 222-282, respectively.

[9]There was in fact no evidence presented at trial regarding California or any other state's actual manner of conducting the hearings supervised either by Mr. Carter or Mr. Streett.

nation-wide involving voluntary leave or misconduct issues. (R.T., pp. 191-194.)

Mr. Streett testified that he is the supervisor of the appeals unit for the United States involving benefit eligibility hearings after benefits have been denied. (R.T., pp. 222-226.) His function is to review and offer guidance and assistance to state programs. (R.T., p. 224.) His office evaluates the quality of the states' benefit eligibility hearings and offers a training program in hearings and decision writing to the states. (R.T., p. 228.) He further testified that federal guidelines are provided to the states as to how these particular hearings should be conducted and how particular fact patterns may be adjudicated. (R.T., pp. 226-227.) Mr. Streett testified that the guidelines are general, intended to cover all hearings, and that they do not specifically refer to church employees and church institutions. (R.T., p. 232.)

Burden of Unemployment Compensation Tax Program on Appellees.

At trial, the Grace Brethren appellees presented testimony by Mr. Enderlin, the superintendent of Redwood Christian Schools (one of the Grace Brethren appellees) and Mrs. Brandwood, a parent of students attending Redwood Christian Schools. Mrs. Brandwood is also a Grace Brethren appellee. Both witnesses' testimony pertained to their reasons for opposing the inclusion of Redwood Christian Schools in the federal-state unemployment compensation tax program and in particular to the burden such program would place upon them. (R.T., pp. 7-82; 113-115.)

Mr. Enderlin testified that a very important reason his school was opposed to the imposition of the unemployment compensation tax is the financial aspect of the program. (R.T., pp. 43-45.) Mr. Enderlin testified that with respect to minimum wage and workers' compensation laws his

school would not comply with those laws if the cost of compliance rose to a point above that which would be acceptable to the school. (R.T., pp. 40-42; 70-73.) In addition, with respect to fire, safety, sanitation and health regulations imposed by governmental bodies, Mr. Enderlin indicated that his school did not oppose such regulations because they help to advance the school's religious mission and because there had not yet been any unreasonable demands. (R.T., pp. 30-31.)

Mr. Enderlin also testified that his schools have a disability insurance program for its employees (R.T., pp. 50-52), the schools do not participate in social security (R.T., p. 36), and they do not receive any form of local, state or federal financial assistance. (R.T., p. 36.)

Mrs. Brandwood testified that her opposition to the imposition of the unemployment compensation tax was financially related in that her tuition would have to increase in the event the program was extended to cover Redwood Christian Schools. (R.T., p. 115.) She also indicated that she felt that the imposition of the tax might lead to unfavorable teachers being allowed to teach at the school. (R.T., p. 115.)

The District Court's Decision.

Following the submission of post-trial briefs, the District Court held *inter alia* that excessive entanglement of church and state was inevitable during the benefit eligibility determination process if religious schools were brought within the scope of the unemployment compensation tax program. Therefore, the District Court concluded that both 26 U.S.C. § 3309(b) and California Unemployment Insurance Code § 634.5(a) were unconstitutional as applied. (State J.S. App. A, pp. 25-33, 44 footnote 39; App. B, pp. 45-48; App. C, pp. 49-51.)

The District Court also concluded in its Second Supplemental Opinion that no violation of the Free Exercise Clause results from the inclusion of employees of religious schools in th unemployment compensation tax program because the burden or injury complained of by the appellees was purely financial in nature. (State J.S. App. A, pp. 16-25.)

Finally, the District Court declined to reach the merits of the Grace Brethren appellees' equal protection argument since the Court had already determined that application of the unemployment compensation tax program to their employees involved impermissible entanglement of the state with religion. (State J.S. App. A, pp. 33-35.)

SUMMARY OF ARGUMENT.

This Court has jurisdiction of this appeal under 28 U.S.C. § 1252 because the *basis* of the District Court's decision was that both 26 U.S.C. § 3309(b) and California Unemployment Insurance Code § 634.5(a) were unconstitutional as applied to the appellees. The District Court was fully cognizant of the interplay between state and federal unemployment compensation tax programs. The only evidence before the District Court pertained to general *federal* guidelines regarding the benefit eligibility hearings and not specifically California procedures.

No potential for excessive entanglement in the benefit eligibility determination process was demonstrated by the appellees. The evidence produced at trial was far too speculative to support the District Court's contrary conclusion. The focus in a benefit eligibility hearing is upon the activities of the employee and whether there was a wilful violation of an established work rule. The religious beliefs of the respective parties is irrelevant as is whether the given work rule conforms to church doctrine. The benefit eligibility determination process is constitutional under the standards

set forth in the church property dispute cases decided by this Court.

No violation of the Free Exercise Clause results from the inclusion of employees of religious schools in the unemployment compensation tax program. There is no constitutional right to exemption from taxes for appellees. As the only burden or injury complained of by the appellees was purely financial in nature, when balanced against the important public policy served by the unemployment compensation tax program, the conclusion is compelled that no Free Exercise rights are violated.

No violation of the Equal Protection Clause results from the inclusion of employees of unaffiliated religiously oriented schools in the unemployment compensation tax program. A classification of employers according to church affiliation rather than by religious mission or curriculum content avoids potential impermissible governmental entanglement. The classification of employers set forth in 26 U.S.C. § 3309(b) and California Unemployment Insurance Code § 634.5(a) reflects a congressional attempt to accommodate sincerely held religious beliefs against the need of their employees for protection against wage loss in much the same way as 26 U.S.C. § 1402(g).

The United States was an indispensable party to these actions in that without its joinder appellees could not have obtained complete relief. Therefore, as the United States cannot be compelled to submit to state court jurisdiction, the state remedy for appellees was not plain, speedy and efficient for purposes of 28 U.S.C. § 1341.

ARGUMENT.

I.

Introductory Statement.

The State has appealed from that portion of the District Court's judgment which finds impermissible and excessive entanglement with religion in the benefit eligibility determination process with respect to religious schools. (Second Supplemental Opinion, State J.S. App. A, pp. 25-33.) This issue was expressly not considered by this Court in *St. Martin Evangelical Church, et al. v. South Dakota* (1981) ... U.S. ..., 68 L.Ed.2d 612, 624. The State is in full agreement with the District Court in its granting of declaratory relief on purely statutory construction grounds as to the Category 1 and 2 religious organizations.[10] Rather, the focus of this appeal is on that portion of the judgment which relates to the finding of excessive entanglement with religion in relation to the benefit eligibility determination process. As will be demonstrated below, the evidence produced at trial was far too speculative and does not support such a finding.

II.

The Basis of the District Court's Judgment Was That Both 26 U.S.C. § 3309(b) and California Unemployment Insurance Code § 634.5(a) Were Unconstitutional as Applied. Therefore, Jurisdiction Is Properly Invoked Under 28 U.S.C. § 1252.

On November 2, 1981, the Court agreed to hear the appeals by the State, United States and Grace Brethren appellees but postponed further consideration of jurisdiction

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[10]Likewise, this Court's holding in *St. Martin* is in complete accord with the State's position on the issues considered therein. The State in fact filed an *amicus curiae* brief urging such a holding.

to the hearing of the cases on the merits. As the discussion below will indicate the Court's jurisdiction is properly invoked under 28 U.S.C. § 1252 because the *basis* of the District Court's decision was that *both* an Act of Congress *and* its state analogue were unconstitutional as applied. *United States v. Raines* (1960) 362 U.S. 17, 20.

28 U.S.C. § 1252 is not to be read restrictively. As this Court held in *Reid v. Covert* (1956) 351 U.S. 487, opposite conclusions on merits reached on rehearing (1957) 354 U.S. 1:

> "[I]t would do violence to the purpose of Congress to provide a 'prompt review of the constitutionality of federal acts,' (Citation), to interpret § 1252 restrictively." (*Reid v. Covert, supra,* 351 U.S. 487, 490.)

It is sufficient under 28 U.S.C. § 1252 if the federal statute was held unconstitutional as applied to the circumstances of the particular case. *United States v. Darusmont* (1981) ... U.S. ..., 66 L.Ed.2d 513, 515.

In the instant matter, although the Order and Judgment in the Grace Brethren case speaks in terms of only the California statute being unconstitutional as applied, a review of the District Court's opinion makes it evident that the District Court's conclusion was not so restrictive. (State J.S. App. A, pp. 25-33; App. B, pp. 46-47.)

Specifically, the District Court was well aware of the coordinated nature of the federal-state unemployment compensation tax program. The District Court recognized the "overwhelming pressure" the United States is able to exert over a state such as California to conform its actions to the federal guidelines through the conformity process embodied in 26 U.S.C. § 3304(c). (State J.S. App. A, pp. 36-37;

App. D, pp. 55-57.)[11] This "pressure" exists in benefit eligibility determinations as well in that denial of benefits for employees discharged for misconduct connected with their work is provided both in 26 U.S.C. § 3304(a)(10) and correspondingly in California Unemployment Insurance Code § 1256.

As was indicated in the Statement of Case, the only evidence presented to the District Court on the benefit eligibility issue was the testimony of *federal* witnesses, unfamiliar with California procedures and definitions, applying *federal* guidelines to hypotheticals posed to them by the various parties. No evidence of the specific California application of California Unemployment Insurance Code § 634.5(a) in benefit eligibility hearings was ever presented to the Court.

Although the District Court only referred to the California statute in its Order and Judgment, that conclusion was based upon an analysis of the identical federal statute. (State J.S. App. A, pp. 25-33.)[12] The District Court's language in its Second Supplemental Opinion is particularly helpful in this context:

> "Since such entanglement is inevitable during the benefit eligibility determination process if religious

[11]This Court recognized the "intertwined" nature of the federal-state unemployment compensation law in *St. Martin* at 68 L.Ed.2d 612, 618-619, fn. 9.

[12]*Cf. Williams v. Zbaraz* (1980) 448 U.S. 358, 365-7. In *Williams, unlike the present case*, only the state statute was challenged by the plaintiffs. Nevertheless, the District Court in *Williams* noted that the same reasoning would apply in determining the constitutional validity of both the federal and state statutes. This Court held that the appeal under 28 U.S.C. § 1252 was proper even though the District Court exceeded its jurisdiction in finding the federal statute unconstitutional because no case or controversy was presented and even though all of the relief sought by plaintiffs could have been awarded entirely on the basis of the District Court's ruling on the *state* statute. Unquestionably, in light of *Williams*, the instant appeal is quite properly taken.

> schools are brought within the scope of the *unemployment compensation tax scheme*, constitutional considerations bar the application of the *scheme* to them." (State J.S. App. A, p. 33.) (Emphasis added.)

To further demonstrate that the District Court indeed was holding the federal statute unconstitutional as applied as well, footnote 39 of the Second Supplemental Opinion removes any remaining doubt:

> "At this time, the Court has no information indicating what response, if any, the Secretary will make to the Court's conclusion that the state defendants may not constitutionally impose the state unemployment compensation tax scheme on the Category 3 employees of non-church-affiliated schools. Since such employees were, under any construction of the relevant statutes, subject to the unemployment compensation scheme, the Secretary concentrated his attention on the Category 1 and 2 employees, whose status his erroneous statutory interpretation affected. If the Secretary, in response to failure by the state defendants to collect unemployment compensation taxes on behalf of Category 3 employees, institutes decertification proceedings against the State of California, the parties may apply to this Court for further relief." (State J.S. App. A, p. 44.)

Notwithstanding the fact that the State is the entity in the unemployment compensation tax "scheme" which actually conducts the benefit eligibility hearings, the District Court was well aware that it was not acting independently of the United States. It was the application of *both* the *federal and state* statutes which the District Court found objectionable and upon which its decision was based. Thus, jurisdiction is properly invoked under 28 U.S.C. § 1252.

III.

No Potential for Excessive Entanglement in the Benefit Eligibility Determination Process Has Been Shown.

As has been repeatedly noted herein, the evidence presented at trial regarding entanglements in the benefit eligibility determination process consisted solely of hypothetical questions and the responses thereto by federal witnesses. There was no evidence that any of the situations suggested in the questions have occurred or will ever occur. Such a showing is simply too speculative when balanced against the extreme importance of unemployment benefits for the employees of these religious organizations. This Court has held that a limited judicial review is permissible in church property disputes. The benefit eligibility determination process would easily fall within the confines of said permissible review.

This Court has announced a three-part test for determining whether a statute is permissible under the Establishment Clause of the First Amendment of the United States Constitution. *Lemon v. Kurtzman* (1971) 403 U.S. 602, 612-13. If a statute violates any of the three parts it must be struck down under the Establishment Clause. *Stone v. Graham* (1980) ... U.S. ..., 66 L.Ed.2d 199, 202. The third part of the test is whether the statute fosters an "excessive government entanglement with religion." *Lemon v. Kurtzman, supra*, 403 U.S. 602, 613. This test is inescapably one of degree. *Walz v. Tax Commission* (1970) 397 U.S. 664, 674. Total separation between church and state is not possible nor is it required. Some relationship between government and religious organizations is inevitable. *Lemon v. Kurtzman, supra*, 403 U.S. 602, 614. The Religion Clauses must not be construed with a literalness that would undermine the ultimate constitutional objective as illuminated by history. *Walz v. Tax Commission, supra*, 397 U.S. 664,

671. Of course, the mere potential of *excessive* entanglement is sufficient to offend the First Amendment. *Meek v. Pittenger* (1975) 421 U.S. 349, 371-72; *Lemon v. Kurtzman, supra*, 403 U.S. 602, 615, 619-20; *Catholic Bishop v. NLRB* (7th Cir., 1977) 559 F.2d 1112, 1126, *aff'd.* 440 U.S. 490 (1979). However, the entanglement truly must be *excessive*. The State submits that any entanglement which might occur in the benefit eligibility determination process would be, at most, *de minimis* and thus permissible under the Religion Clauses.

As was carefully and accurately pointed out by the District Court below, the unemployment compensation process involves two separate procedures: (1) a determination as to whether a certain employer is subject to unemployment insurance in the first instance (tax determination) and (2) a determination as to whether a specific employee is eligible for benefits (benefit determination). (State J.S. App. A, pp. 25-26.)

The instant cases originated as a challenge to the imposition of the unemployment insurance tax upon religious schools, *not* as a challenge to an award of benefits to any religious school employee. Since these cases proceeded on the *tax* side of the unemployment compensation process, the record below consists exclusively of declarations, documentation and oral testimony which are related only to the *tax* determination procedure. There was no evidence presented by the appellees that there ever had been a benefit eligibility determination hearing with respect to an employee of a church-related school, much less an actual hearing which necessitated inquiry into church doctrine. The only evidence at trial pertaining to this issue was in the form of hypothetical questions and answers posed to two witnesses for the federal defendants. That which is important though is that although each witness was experienced in the field

of benefit eligibility determination hearings, both witnesses testified that they had *never* conducted, attended nor read a transcript of a benefit eligibility hearing where the issues involved a dispute between a church and church employee with respect to the reasons for the discharge of the employee by the church. (R.T., pp. 165-166; 228-232.)

Unemployment coverage of employees of church-related schools is not a new phenomenon. Parochial elementary and secondary school employees universally were covered under the temporary Special Unemployment Assistant Program ("SUA"; P.L. 93-567, 88 Stat. 1850) from 1974 through 1977, and have since been covered under FUTA in the states which adopted (prior to the *St. Martin* case) the Secretary of Labor's interpretation. Employees of church-related colleges have been covered since 1972. Furthermore, Mr. Carter's testimony indicated that in 1979 alone there were approximately 4 million cases adjudicated nation-wide at the predetermination benefit eligibility hearing stage involving voluntary leave or misconduct issues. (R.T., pp. 191-194.) Yet, there was no evidence that even one of these cases involved a dispute between a religious organization and its employee which necessitated an inquiry into church doctrine or which involved the reasons for the discharge of the employee. Surely, appellees' showing is insufficient to sustain the District Court's conclusion on this issue.

An additional point must be noted that under California law, a determination under the tax side is not necessarily binding on any determination under the benefit side and vice versa. The leading case is *Empire Star Mines, Inc. v. California Employment Commission* (1946) 28 Cal.2d 33, 68 P.2d 686, where the California Supreme Court stated:

> "But there is no basis for the attorney general's contention that because the legislation confers benefits . and also imposes taxes, the two parts of the law are

> inextricably connected. The taxing sections of the legislation are entirely separate from those concerning benefits, and although the benefits are paid from the amount collected as taxes imposed by the act, the provisions fixing liability for payments to the fund are to be considered accordingly." (*Empire Star Mines Co. v. Cal. Emp. Com., supra,* 28 Cal.2d 33, 43.)

The *Empire Star Mines* case dealt with the question of whether or not certain persons who performed services for the Empire Star Mines Company were employees or independent contractors. If these persons were employees, then Empire Star Mines would be subject to the unemployment insurance taxes of California, and its employees would be eligible for unemployment compensation benefits. The language quoted was the court's response to the state's argument that since the individuals who had performed services for Empire Star Mines had already been adjudged to be employees and were awarded unemployment compensation benefits by the California Employment Commission in an administrative proceeding dealing with the benefit issues that had become final, the California Supreme Court was precluded from a finding on the *tax issue* that would be contrary to that administrative result. In California, a determination by the State with regard to benefit eligibility is separate and distinct from a determination by the State with regard to whether or not an employer is subject to the unemployment insurance tax, and each determination may be challenged by the parties in separate proceedings. See California Unemployment Insurance Code §§ 1221 *et seq.* and 1326 *et seq.* It is clear that the California Supreme Court felt that the issue of liability for the unemployment insurance tax could and should be considered independent of any benefit determination involving the employees of the subject employer.

The State is not suggesting that this Court ignore the potential for excessive entanglement in benefit eligibility hearings. Rather, the State submits that this Court should recognize the separateness of the two procedures and in determining the propriety of the exemption from unemployment insurance tax for unaffiliated religious organizations, should require concrete proof of such excessiveness and not rely upon mere hypothetical assertions.

In a benefit eligibility hearing, the purpose is to decide whether a particular employee will receive unemployment benefits. The State is not concerned with the religious beliefs of either the employer or employee. In determining whether an employee was discharged for misconduct the important factor is whether such employee failed to abide by an established work rule. Employers such as the appellees herein are of course free to establish any work rules they desire, including rules incorporating religious beliefs. A knowing violation of a work rule constitutes misconduct. The principal inquiry in a benefit eligibility hearing is not whether a given work rule conforms to Church doctrine but only whether the employee knew of the rule and nevertheless violated it.[13] The benefit eligibility hearing could be con-

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[13]*Maywood Glass Co. v. Stewart* (1959) 170 Cal.App.2d 719, 724, 339 P.2d 611; *Rowe v. Hansen* (1974) 41 Cal.App.3d 512, 521, 116 Cal.Rptr. 16; *Davis v. Unemployment Ins. Appeals Bd.* (1974) 43 Cal.App.3d 71, 75, 117 Cal.Rptr. 463; *Drysdale v. Department of Human Resources Development* (1978) 77 Cal.App.3d 345, 352-3, 142 Cal.Rptr. 495. The test for misconduct is essentially volitional. The focus is on the employee's acts rather than the reasonableness of the work rule or the extent of economic consequences to the employer. Indeed, the mere "flouting" of the employer's authority is sufficient harm to the employer to constitute misconduct if the work rules have been knowingly violated. *Rowe v. Hansen, supra,* 41 Cal.App.3d 512, 523.

The actual reasonableness of a given work rule is rarely the subject of inquiry. However, an employee is not required to comply with a work rule which is considered to be unreasonable in the following *limited* instances as set forth in Title 22 California Administrative Code

(footnote continued on following page)

ducted on a purely *secular* basis. As such the process clearly would not be violative of the First Amendment notwithstanding the religious nature of the employer. *United Methodist Council v. Superior Court* (1978) 439 U.S. 1369, 1371 (Rehnquist, J., in chambers).

This Court has decided a line of cases in recent years relating to church property disputes and the role civil courts may play therein. *Jones v. Wolf* (1979) 443 U.S. 595; *Serbian Orthodox Diocese v. Milivojevich* (1976) 426 U.S. 696; *Maryland & Va. Churches v. Sharpsburg Church* (1970) 396 U.S. 367; *Presbyterian Church v. Hull Church* (1969) 393 U.S. 440. The principles developed therein are helpful and have been held to apply with equal force to church disputes over church polity and church administration. *Serbian Orthodox Diocese v. Milivojevich, supra*, 426 U.S. 696, 710.

From the above cases, it is well settled that the First Amendment prohibits civil courts from resolving church

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Section 1256-36(b)(1) (State J.S. App. K, pp. 97-98):

1. The rule is unreasonable because compliance is impossible due to physical limitations of the employee.
2. The rule is unreasonable because compliance would impose a new and unreasonable burden on the employee.
3. The rule is unreasonable because it does not relate to or affect the employer's business interest.
4. The rule is unreasonable because the employee reasonably believes that compliance would result in a violation of a law.
5. The rule is unreasonable because the employee reasonably believes compliance would cause an undue risk of injury or illness.
6. The rule is unreasonable because the employee had a reasonable doubt of the authority of the individual issuing the order.

The above regulation was promulgated pursuant to California Unemployment Insurance Code §§ 305 *et seq.* in order to enforce the provisions of Section 1256 of the California Unemployment Insurance Code.

It should be noted that the context in which an employee is not required to comply with a work rule under the above regulation is far removed from the situation presented in the instant matter.

disputes on the basis of religious doctrine and practice. *Jones v. Wolf, supra*, 443 U.S. 595, 602; *Serbian Orthodox Diocese v. Milivojevich, supra*, 426 U.S. 696, 710; *Maryland & Va. Churches v. Sharpsburg Church, supra*, 396 U.S. 367, 368; *Presbyterian Church v. Hull Church, supra*, 393 U.S. 440, 449. As a corollary to this commandment, the Amendment requires that civil courts defer to the resolution of issues of religious doctrine or polity by the highest court of a hierarchical church organization. *Jones v. Wolf, supra*, 443 U.S. 595, 602; *Serbian Orthodox Diocese v. Milivojevich, supra*, 426 U.S. 696, 724-5. The First Amendment, however, does not dictate that a state must follow a particular method of resolving church disputes. *Jones v. Wolf, supra*, 443 U.S. 595, 602. Indeed, a state may adopt *any* one of various approaches for settling church property disputes so long as it involves no consideration of doctrinal matters. *Maryland & Va. Churches v. Sharpsburg Church, supra*, 396 U.S. 367, 368 (Brennan, J., concurring). One of the approaches this Court has found to be constitutionally permissible is the neutral-principles approach. *Jones v. Wolf, supra*, 443 U.S. 595, 602-3; *Maryland & Va. Churches v. Sharpsburg Church, supra*, 396 U.S. 367, 368 (Brennan, J., concurring).

In the *Maryland & Va. Churches* case, the Court of Appeals of Maryland was permitted to settle a local church property dispute on the basis of the language of the deeds, the terms of the local church charters, the state statutes governing the holding of church property and the provisions of the constitution of the general church concerning the ownership and control of church property. 396 U.S. at 368.

Also, in *Jones v. Wolf, supra*, 443 U.S. 595 this Court reaffirmed the neutral-principles analysis and further indicated that it was constitutionally permissible to require the interested parties to modify the deeds, charters or church

constitution in order to ensure that a certain result would be reached by the civil courts adjudicating the dispute. The burden involved in taking such steps was held to be minimal. *Id.* at 606. Civil courts would be bound to give effect to the result indicated by the parties provided it is embodied in some legally cognizable form. *Ibid.*

Similarly, in a benefit eligibility hearing it would not be an unconstitutional burden to require the interested parties to prove what the work rule in question was. Under California law, the *employer* would have the burden of proving what the work rule was and that the employee knowingly violated it. *Maywood Glass Co. v. Stewart, supra*, 170 Cal.App.2d 719, 724-5; California Unemployment Insurance Code § 1256.

Once the religious employer demonstrated what was the work rule or church doctrine alleged to have been violated, the State would be bound to give effect to that work rule or church doctrine. *Jones v. Wolf, supra*, 443 U.S. 595, 606.

In determining whether there was a "knowing violation" of the work rule (or church doctrine as the case may be), the State would *not* be foreclosed from determining the *existence* of the individual's religious belief or understanding of the church doctrine. The State would be foreclosed from determining the *truth* of that belief or understanding. *United States v. Seeger* (1968) 380 U.S. 163, 185.

The distinction between adjudicating the employee's *understanding* of church doctrine versus the doctrine itself is crucial. Only the former would need to be adjudicated in a benefit eligibility hearing. This adjudication would be plainly permissible under this Court's recent holding in *Thomas v. Review Bd. of Indiana Employment Sec.* (1981) ... U.S. ..., 101 S.Ct. 1425, 1430-1431. Under *Thomas*,

the State would be allowed to determine whether the employee had terminated his or her employment because of an *honest conviction* that such work was forbidden by his religion. *Id.* at 1431. However, it would not be within the competence of the State or the judiciary to inquire whether the employee or someone else more correctly perceived the commands of their common faith. *Ibid.* The State would not be permitted to become an "arbiter of scriptural interpretation." *Ibid.* Nonetheless, *Thomas* indicates that without violating the Religion Clauses, the State could adjudicate the employee's *understanding* of the work rule or church doctrine.

Furthermore, it has been held that the Religion Clauses do not prevent a civil court from independently examining and making the ultimate decision regarding the structure and actual operation of a hierarchical church and its constituent units. *United Methodist Council v. Superior Court, supra,* 439 U.S. 1369, 1372 (Rehnquist, J., in chambers). In *United Methodist,* Justice Rehnquist continued stating:

> "There are constitutional limitations on the extent to which a civil court may inquire into and determine matters of ecclesiastical cognizance and polity in adjudicating intra-church disputes. See *Serbian Eastern Orthodox Diocese v. Milivojevich.* But this Court never has suggested that those constraints similarly apply outside the context of such intra-organization disputes. Thus, *Serbian Eastern Orthodox Diocese* and other cases cited by applicant are not in point. Those cases are premised on a perceived danger that in resolving intra-church disputes the State will become entangled in essentially religious controversies or intervene on behalf of groups espousing particular doctrinal beliefs. 426 U.S. at 709-710. *Such considerations are not applicable to purely secular disputes between third parties and a particular defendant, albeit a religious af-*

filiated organization, in which fraud, breach of contract, and statutory violations are alleged." *Id.* at 1372-3. (Emphasis added.)

The benefit eligibility hearing could conceivably be analogized to a breach of contract adjudication in that the employer is in essence alleging that the employee knowingly violated his or her "contract of employment." The proceeding would be purely *secular* with no necessity to interpret or weigh church doctrine. *Cf. Presbyterian Church v. Hull Church, supra,* 393 U.S. 440, 450. The only issue to be resolved would be whether the employee failed to abide by an established work rule. The potential for any impermissible or excessive entanglement between church and state is genuinely lacking.

Finally, this Court has recognized an exception to the rule that civil courts shall not disturb the decisions of the highest ecclesiastical tribunal within a church of hierarchical polity in their application to the religious issues of doctrine or polity before them. *Jones v. Wolf, supra,* 443 U.S. 595, 609, fn.8; see also *United Methodist Council v. Superior Court, supra,* 439 U.S. 1369. If the decision of the religious tribunal was the product of fraud or collusion "marginal civil court review" of that decision would be permissible. *United Methodist Council v. Superior Court, supra,* 439 U.S. 1369; *Serbian Orthodox Diocese v. Milivojevich, supra,* 426 U.S. 696, 713. In fact, this Court has seemingly left open the question whether in addition to the above instances when a church tribunal "act(s) in bad faith for secular purposes", a limited exception may exist for an arbitrary decision by the church tribunal. See *Serbian Orthodox Diocese v. Milivojevich, supra,* 426 U.S. 696, 713.

The State is not suggesting that the decision of a religious employer to terminate an employee would be the product of fraud, collusion or arbitrariness. Nonetheless, that which

is important is that this Court has permitted in those instances a "marginal civil court review" of decisions of church tribunals on matters which are *purely ecclesiastical*. In a benefit eligibility hearing, there would *never* be a necessity to review the religious employer's interpretation of its doctrine or work rules. Unquestionably, under the requisite close scrutiny of the *degree* of entanglement involved in the relationship, there would be absolutely no potential for excessive governmental entanglement with religion. See *Lemon v. Kurtzman, supra*, 403 U.S. 602, 614.

IV.

No Violation of the Free Exercise Clause Results From the Inclusion of Employees of Religious Schools in the Unemployment Compensation Tax Program.

Appellees contend that the District Court erred in finding that the inclusion of employees of religious schools in the unemployment compensation tax program results in no violation of the Free Exercise Clause. The State respectfully disagrees with the appellees. The law and the facts of this case plainly support the District Court's findings. The arguments put forth herein by the appellees were fully considered and properly rejected by the District Court. (State J.S. App. A, pp. 16-25.)

In considering appellees' arguments below, the District Court correctly observed that the injury to the Free Exercise rights asserted by the appellees ultimately comes down to the *financial* burden imposed by the extension of the unemployment compensation tax to these schools. (*See*, State J.S. App. A, pp. 20-21, 25-26.) Indeed, the Grace Brethren appellees' chief witness, Mr. Enderlin, the superintendent of Redwood Christian Schools testified below that a very important reason his school is opposed to the imposition of the unemployment compensation tax is the *financial* aspect

of the program. (R.T., pp. 43-45.) Consistent therewith, the superintendent also testified that with respect to minimum wage and worker's compensation laws his school would *not* comply with those laws if the *cost of compliance* rose to a point *above* that which would be acceptable to the school. (R.T., pp. 40-42; 70-73.) Mr. Enderlin also indicated that his schools complied with fire, safety, sanitation and health regulations imposed by governmental bodies because they help to advance the schools' religious mission *and because there had not yet been any unreasonable demands*. (R.T., pp. 30-31.)

Further, the testimony of another appellee, Mrs. Brandwood, a parent of students attending Redwood Christian Schools, indicated that her opposition to the imposition of the unemployment compensation tax was *financially* related in that her tuition would have to increase in the event the program was extended to cover Redwood. (R.T., p. 115.)

In all, the evidence presented below plainly demonstrated that the burden or injury complained of by the appellees was purely financial in nature.[14] As the District Court correctly noted "there [was] no suggestion that the extension of the tax to religious schools would abridge rights to the free exercise of religion in any fashion *independent* of the financial burden which accompanies any tax." (State J.S.

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[14]The District Court correctly pointed out (State J.S. App. A, pp. 22-23) that the "burden" the unemployment compensation tax imposes upon a non-profit employer such as appellees is *indirect* in that the employer may elect the "reimbursement method" of contribution and thus contribute only the amounts of benefits actually found due to its former employees who have been or are discharged. *See*, 26 U.S.C. §§ 3303(e), 3309(a)(2) and California Unemployment Insurance Code §§ 801 *et seq*. In the alternative, the employer may choose the "tax rate" method and contribute according to the number of employees and his past employment history. *See*, 26 U.S.C. § 3302(a)(1) and California Unemployment Insurance Code §§ 901 *et seq*. and 976 *et seq*. Clearly, the opportunity to select either method of contribution minimizes the financial impact upon the employer.

App. A, p. 20.) This Court has noted previously that the mere fact that a statute renders the practice of religion more expensive is not, by itself, sufficient to bring the statute into conflict with the Free Exercise Clause. *Braunfeld v. Brown* (1961) 366 U.S. 599, 605; *Johnson v. Robison* (1974) 415 U.S. 361, 383-5 (argument rejected that the withholding of educational benefits from a conscientious objector violated the free exercise rights of the objector). There is no constitutional right to exemption from taxes for the appellees. *Follett v. McCormick* (1944) 321 U.S. 573, 578; *Murdock v. Pennsylvania* (1943) 319 U.S. 105, 112.

Moreover, it is without dispute that religiously based activities "are often subject to regulation by the States in the exercise of their undoubted power to promote the health, safety, and general welfare, or the Federal Government in the exercise of its delegated powers." *Wisconsin v. Yoder* (1972) 406 U.S. 205, 220. *See, Gillette v. United States* (1971) 401 U.S. 437 (conscientious objector exemption statute upheld); *Braunfeld v. Brown, supra,* 366 U.S. 599 (mandatory Sunday closing law applicable to Orthodox Jewish merchants); *Prince v. Massachusetts* (1944) 321 U.S. 158 (child labor law applicable to religious organizations); *Reynolds v. United States* (1879) 98 U.S. 145 (polygamy statutes applicable to religious organizations which sanctioned such activities).

Neutral legislation which is far more burdensome upon the practice of religion than that which is present in the instant case has been upheld by this Court where important public policies are at stake. *Committee For Public Education And Religious Liberty v. Regan* (1980) 444 U.S. 646, 659-661; *Prince v. Massachusetts, supra,* 321 U.S. 158.

Furthermore, appellees' argument that excessive entanglement results from the routine duty under the unemployment compensation tax program to keep accurate employ-

ment records and make related reports to the State must be rejected in that the recordkeeping involved herein is far less extensive than that which was recently sustained against similar charges in *Committee For Public Education And Religious Liberty v. Regan, supra,* 444 U.S. 646, 659-661. *See also, United States v. Holmes* (5th Cir., 1980) 614 F.2d 985 (Internal Revenue Service summons enforced as to a bishop and director of a church as against a First Amendment challenge. The Court balanced the incidental burden on the church against the interest of government in its fiscal integrity).

Finally, the District Court correctly pointed out that there is indeed a compelling secular governmental interest in providing unemployment compensation to unemployed individuals. (State J.S. App. A, pp. 24-25.) *See*, California Unemployment Insurance Code § 100, which lists the secular purposes for which California adopted its own unemployment compensation program. Further, this Court has recognized the extreme importance of unemployment benefits. *California Department of Human Resources v. Java* (1971) 402 U.S. 121, 131-2 ("Unemployment benefits provide cash to a newly unemployed worker, 'at a time when otherwise he would have nothing to spend,' serving to maintain the recipient at subsistence levels . . ."). When this compelling interest is balanced against the indirect, purely financial burden which the unemployment compensation tax program imposes upon the appellees, the conclusion is inescapable that no violation of the Free Exercise Clause results from the inclusion of the employees of religious schools in the unemployment compensation tax program.

V.

No Violation of the Equal Protection Clause Results From the Inclusion of Employees of Unaffiliated Religiously Oriented Schools in the Unemployment Compensation Tax Program.

Although the District Court did not reach the question whether to deny the exemption provided in 26 U.S.C. § 3309(b) and California Unemployment Insurance Code § 634.5(a) to the Category 3 religious organizations because of their lack of formal church affiliation would be a denial of equal protection, the Court did consider and discuss the issue. In its Second Supplemental Opinion, the District Court suggested that a constitutionally permissible classification of employers could be by religious mission and curriculum content rather than by formal church affiliation.[15] (State J.S. App. A, p. 35.) The State submits that to heed the District Court's suggestion would unquestionably lead to more entanglement between church and state in that it would be virtually impossible for the state to make the determination of the existence of a sufficiently religious mission or curriculum without the constant monitoring abhorred by this Court in *Lemon v. Kurtzman, supra*, 403 U.S. 602, 627 (Douglas, J., concurring).[16]

It is beyond dispute that a tax exemption is a matter of legislative grace and the taxpayer has the burden of es-

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[15]The classification of employers for purposes of FUTA has long been held to be constitutionally permissible. *Carmichael v. Southern Coal & Coke Co.* (1937) 301 U.S. 495, 508-512.

[16]*Cf. Thomas v. Review Bd. of Indiana Employment Sec., supra*, ... U.S. ..., 101 S.Ct. 1425, 1432, where this Court rejected the argument put forth in support of the Indiana benefit eligibility procedures, that the procedures would avoid detailed probing by *employers* in job applicants' religious beliefs. Unlike *Thomas*, the "probing" which would result in extending the exemption as suggested by the District Court, would be by the *government* and thus be much more *direct*.

tablishing its entitlement to the exemption. *Dickinson v. United States* (1953) 346 U.S. 389, 394-5. As the Eighth Circuit of the United States Court of Appeals has indicated, the receiving of an exemption is *not* a constitutional right for a religious organization. *Parker v. Commissioner of Internal Revenue* (8th Cir., 1966) 365 F.2d 792, 795, *cert. den.* 385 U.S. 1026. Specifically, the Court stated:

> "Since the government may constitutionally tax the income of religious organizations, it follows that the government may decide not to exercise this power and grant reasonable exemptions to qualifying organizations, while continuing to tax those who fail to meet these qualifications. The receiving of an exemption is thus a matter of legislative grace and not a constitutional right. As long as exemptions are denied by the Commissioner on a non-discriminatory basis using specific and reasonable guidelines and *without inquiry into the merits of the particular religious doctrines*, the withholding of religious exemptions is permissible under the Constitution." (Emphasis added.) (Footnote omitted.) (*Id.* at 795.)

Obviously, the Classification of employers according to church affiliation rather than on some other basis satisfies the Eighth Circuit's criteria and avoids the "inquiry into the merits of the particular religious doctrines."

An analogous situation exists under 26 U.S.C. § 1402(g) which provides an exemption from social security taxes for a "recognized religious sect" which by reason of the tenets of the sect is opposed to the receipt of social security benefits and agrees to waive them. Further, the Secretary of Health, Education and Welfare must find that the sect makes reasonable provision for its dependent members. This Court expressed no objection to this exemption statute in *Wisconsin v. Yoder, supra*, 406 U.S. 205, 222-3, fn. 11.

In *Jaggard v. Commissioner of Internal Revenue* (8th Cir., 1978) 582 F.2d 1189, *cert. den.* 440 U.S. 913, the Eighth Circuit discussed the purpose of 26 U.S.C. § 1402(g) and rejected an argument by the taxpayer that the requirement of a "recognized religious sect" was unconstitutional and that the exemption should be available to all individuals who meet the other criteria under the statute. The Eighth Circuit stated:

> "Jaggard's argument has been previously considered and rejected by the Tax Court. *Henson v. Commissioner*, 66 T.C. 835, 840 (1976); *Palmer v. Commissioner*, 52 T.C. 310, 314-15 (1969). These cases hold that the purpose of § 1402(g) is neither the advancement nor the inhibition of religion. It represents a congressional attempt to accommodate sincerely held religious beliefs against private and public insurance programs consistent with the overall welfare purpose of the Social Security Act. Congress could reasonably conclude that individuals on their own could not be relied upon to provide for themselves in the event of dependency, but that members of a religious sect who share these views would provide for dependent members. Although in any legislative accommodation of religion there is an inherent balancing of interest, the balance struck here was a constitutionally permissible one. We find the reasoning of these opinions to be dispositive of the issue. Cf. *Wisconsin v. Yoder*, 406 U.S. 205, 222 & n. 11, 92 S.Ct. 1526, 32 L.Ed.2d 25 (1972)." (*Id.* at 1190.)

A similar accommodation of religion was attempted by Congress when it amended FUTA in 1970 to include state law coverage of non-profit organizations. The Senate Report is clear on that point. It provides:

> "Present law. — Under existing Federal law, services performed for non-profit religious, charitable,

> educational and humane organizations and for a State and its political subdivisions are exempt from the tax provisions of the Federal Unemployment Tax Act. There has not, therefore, been a tax-credit incentive for covering employees of these organizations and governments for unemployment compensation purposes. While employment in these organizations and governments is not subject to fluctuations to the same degree as in commerce and industry, unemployment affects a substantial number of their employees, particularly people working in non-professional occupations.
>
> The committee does not want to change the present tax status of non-profit organizations, but is concerned about the need of their employees for protection against wage loss resulting from unemployment . . . Under the reimbursement method of financing, a non-profit organization whose workers experience no compensated unemployment in a year would have no unemployment insurance costs for that year. The committee considers it appropriate that these organizations, which are often dependent upon charitable contributions, should not be required to share in the costs of providing benefits to workers in profit-making enterprises." (S.Rep. No. 91-752, 91st Cong. 2d Sess. 14, reprinted in (1970) U.S. Code Cong. & Ad. News 3606, 3617-18.)

Congress respected the needs of the non-profit organizations but also recognized the tremendous needs of the employees of such organizations for protection against wage loss. Any attempt to remove this protection must be closely scrutinized especially in this period of high unemployment.

The classification of employers provided in 26 U.S.C. § 3309(b) and California Unemployment Insurance Code § 634.5(a) strikes a reasonable balance between sincerely held religious beliefs and protection for employees against

unexpected wage loss. Moreover, it avoids any excessive governmental entanglement with religious entities. As such, there is no denial of equal protection.

VI.

28 U.S.C. § 1341 Should Not Bar This Action.

The United States raised the argument that 28 U.S.C. § 1341 deprived the District Court of subject matter jurisdiction of these cases. The State submits that the United States is in error and that this Court should reach the merits of this controversy.

The basis for the State's argument is that the United States was clearly an indispensable party to these actions in that without its joinder appellees could not have obtained complete relief because of the conformity procedures existing in FUTA. Therefore, as the United States cannot be compelled to submit to state court jurisdiction, the state remedy for appellees was not plain, speedy and efficient for purposes of 28 U.S.C. § 1341.[17] Consequently, there is no jurisdictional bar for this Court to overcome to reach the merits herein.

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[17]It should be noted in this regard that the United States in fact removed the Lutheran case from state court to federal court.

CONCLUSION.

For the foregoing reasons, the State respectfully urges the Court to reverse the judgment of the District Court insofar as it is challenged by the State's appeal.

Respectfully submitted,

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